



West Community
Credit Union

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465 South Kirkwood
Kirkwood, MO 63122

Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314-3428

Dear Members of the Board:

Comments for Proposed Changes to Reg 704—Corporate Credit Union Regulations

Thank you for allowing us to provide our comments regarding the proposed changes to Corporate Credit Union regulations (Reg. 704). While we agree that changes in the rules governing Corporate Credit Unions are necessary, we believe that a material portion of the proposed changes are flawed and could lead to substantially greater hardship on the credit union system. As not-for-profit financial cooperatives, this impact would be felt directly by our members and could diminish the value that credit unions provide to the American consumer.

Overall, the proposed changes will require significant scale for corporate credit unions to survive, and this will certainly lead to consolidation in the system. This seems counter-intuitive to combat the issues that have put us in this position in the first place. Consolidation and scale created corporate credit unions that were “too big to fail” and allowed them to create risks whose financial consequences are now being paid by all federally insured credit unions. It would seem that safety and soundness would be better addressed by regulations that encourage more prudent risk management activities, concentration on core product offerings, and a more diverse system on a smaller scale.

I also believe that some intended consequences may occur as a result of these new regulations.

- Corporates will be forced to lower yields to meet the new net worth requirements thus exacerbating liquidity in the corporate network as NPCU seek higher yields.
- Lower liquidity would have a dramatic impact on the corporates’ ability to systematically retire the legacy assets.
- Forced liquidation of legacy assets will negatively impact the NCUSIF assessments to NPCUs further straining earnings and net worth accumulation.
- NPCUs will look for higher yields and may migrate to a limited number of investment firms thus effectively concentrating NPCU assets with firms outside the reach of our regulators.
- NPCUs that relied on the assistance of their corporates to help direct their investment strategies may go it alone with less experience and sophistication.

To summarize our points, we will address each section of the proposed regulation separately.

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Proposed Section 704.3—Corporate Credit Union Capital

It not likely that most corporates will be able to meet the new capital standards by the first anniversary and will be placed under PCA. The assumptions for the sample investments needed to meet the requirements of the proposed regulation are unrealistic and flawed.

To highlight one example, let's take a look at the assumption that 10% of the portfolio will be allocated to private-label student loans yielding a projected 200 basis points over LIBOR. There are several problems associated with this asset class. Today, private-label student loans are yielding approximately 30 basis points over LIBOR, not 200. Also, private-label student loans are very illiquid and rather difficult to obtain. Finally, private-label student loans are "under scrutiny" as noted in the December 16, 2009, edition of the *Credit Union Times*. To make matters worse, the private-student loans in the sample portfolio provide almost 60% of the 34 basis points projected for the required net interest income!

The difficulty with all of this is that the NCUA used the results of the sample portfolio to conclude that a corporate could achieve a net income position of 21 basis points and meet the net earnings requirement of the proposed rule. We believe the sample portfolio exercise is unrealistic and the resulting conclusion is faulty.

The proposed capital standards are much too stringent for corporates to meet. We believe that this will cause our corporate to shrink its balance sheet and our credit union will have to do the following:

- Move business outside the cooperative network
- Assume more risk as we invest outside the corporate system
- Manage our overnight account on a daily basis
- Wire funds in and out of corporate just to cover settlement
- Forego the valuable Franchise Tax deduction in Missouri for state-chartered credit unions as we invest outside our corporate credit union

This will also cause our corporate to increase earnings and the impact on our credit union will be:

- Higher fees for day-to-day services
- Less yield on investments
- Cost to have our line of credit available to us
- Limited new services available to us
- A reduction in service delivery
- A reduction in educational sessions
- A reduction in credit union sponsorships

This will also most likely require our corporate credit union to merge to remain compliant with the proposed regulations. This would lead to the following negative impacts on our credit union:

- Reduced local control
- Reduced access to corporate decision makers
- Reduced level of personal service and relationships

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- Increased emphasis on sales rather than service resulting in a focus on large credit unions
- Additional capital contributions

The degradation in service levels is a primary concern. Our corporate will have to run so lean in staffing to cut costs to meet the regulations that it will surely hurt service levels. Again, any impact to natural person credit unions directly impacts our members. The reputation and value of credit unions will be diminished and our charter could be at risk in the long run.

Proposed Section 704.4—Prompt Corrective Action

Although we are guarded by the expected increased involvement in corporate credit union affairs by NCUA, we believe these proposed revisions are reasonable.

Proposed Section 704.5—Investments

The proposed revisions, as currently written and under current conditions, are reasonable.

Proposed Section 704.6—Credit Risk Management

The sector limits *seem* reasonable but pose a problem when combined with the tighter single obligor limit and the other limits noted in the ALM section. Excluding certain assets from the sector and obligor limits, like government agency securities, makes sense.

Proposed Section 704.8—Asset and Liability Management

The *limits* placed on average life mismatch and weighted average life in the proposed rule are not reasonable.

The earnings requirements proposed in Section 704.3 seem to require that corporates take more risk in this area than many have taken in the past. However, these proposed limits are *too low* to enable any corporate to achieve the earnings requirements set forth in Section 704.3 regarding capital. *This will force our corporate credit union to pay a much lower rate on overnight deposits and term deposits.*

This will force our credit union to move our term deposits outside the corporate network to bank CDs or marketable securities. In turn, this will cause Missouri credit unions like us, to lose a Franchise Tax deduction and require us to mark-to-market if we choose to invest in marketable securities. This will cause the most harm to small and medium-size credit unions by increasing the complexity (and cost!) of managing their investments.

Proposed Section 704.9—Liquidity Management

The restrictions on borrowing for liquidity purposes seem reasonable but could be an issue for some corporate credit unions.

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Proposed Section 704.11—Corporate Credit Union Service Organizations (CUSOs)

Our corporate credit union will have to receive permission to remain invested in three of our CUSOs, whose services are extremely important to us. If permission is not granted, the proposed rules may present a problem.

Proposed Section 704.14—Corporate Governance

We believe the term limit time frame should be extended from six years to nine years. We also believe the proposed limits on paying legal and other costs for volunteers should be stricken. The proposed limits come from the banking world where directors are paid. We fear this is a step to push this type of regulation on to natural person credit union boards, which would further impact our ability to retain dedicated volunteers.

In Summary

We believe the proposed regulation will force us to turn to banks and other third parties for services currently provided by our corporate credit union, as well as increase the complexity and costs of the services we use today. In the end, the impact to natural person credit unions and our members will be negative and will not lead to a reduction in the systemic risks that NCUA is attempting to address. We encourage NCUA to use the principles of the credit union movement and collaborate with corporate credit unions to craft regulatory changes that positively address all of these concerns. This will not only lead to better safety and soundness in our industry, but it will demonstrate NCUA's willingness to learn from the collective experience of those who manage this business on a day-to-day basis.

I hope that we will have another opportunity for comment once you have received projections on viability of these proposed regulations prior to 2006 and looking forward.

Sincerely,

A handwritten signature in black ink, appearing to read "Gary Hinrichs". The signature is fluid and cursive, with the first name "Gary" and last name "Hinrichs" clearly distinguishable.

Gary Hinrichs
President